



December 1, 2008

Rob Feckner, President  
CalPERS Board of Administration  
P.O. Box 942701  
Sacramento, CA 94229-2701

Dear Mr. Feckner:

I am writing on behalf of the CA Association of School Business Officials (CASBO) to express grave concerns about the proposed regulatory action to add Article 6.5 "Membership" to Title 2 of the California Code of Regulations.

We concur with the comments submitted by CCSESA on November 19, 2008 and the comments submitted by attorney Scott Kivel on November 18, 2008.

In addition, please consider the following comments –

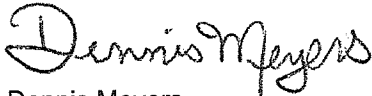
- The IRS has acknowledged that an employee can have a relationship with more than one employer, under the doctrine of co-employment. See, IRS Chief Counsel Advice Memorandum 200415008, which cites Revenue Ruling 66-162. The proposed regulation does not take into account potential co-employment situations that already exist in California and it does not leave CalPERS sufficient discretion to deal with these existing situations and similar circumstances that may arise in the future.
- The IRS has also acknowledged that including employees of a non-profit entity that is established pursuant to state law and is largely controlled by state governmental instrumentalities in a state sponsored, governmental retirement plan will not compromise the federal tax status of the state sponsored, governmental retirement plan. See, IRS Private Letter Ruling 9813019. The proposed regulation does not take into account similar employment relationships that already exist in California and it does not leave CalPERS sufficient discretion to deal with these existing relationships and similar circumstances that may arise in the future.
- In at least one pending case, CalPERS has proposed to deny benefits to individuals who have participated in CalPERS for many years (in some cases, with the knowledge and acquiescence of CalPERS staff), on the basis that these individuals cannot be permitted to participate and must be retroactively denied membership in CalPERS to comply with federal tax laws. To the extent that individuals who do not technically qualify as "employees" under the definition proposed by CalPERS, these individuals are not required to be "kicked out" of CalPERS to correct potential violations of the federal tax Code. The IRS has procedures where a governmental retirement plan can propose suitable corrections to maintain its tax qualified status without necessarily kicking out individuals for whom contributions have been made for many years. See, Revenue Procedure 2008-50, which contains the IRS Employee Plans Compliance Resolution System.

In other contexts, Revenue Procedure 2008-50 allows correction of past eligibility errors by simply amending the retirement plan to include employees who were allowed to participate in error. See, Revenue Procedure 2008-50, Appendix B, section 2.07(3)(a).

Similarly, where leased employees or other individuals who were not common law employees were included in qualified retirement plans, the IRS has exercised its discretion to treat the leased employees or other individuals as employees of the plan sponsor to avoid disqualification of the retirement plan and has effectively excused past violations of the exclusive benefit rule. See, IRS Revenue Procedure 2003-86, section 4.

The proposed regulation provides a harsh, inflexible rule which will not be workable in practice for dealing with existing or future employment relationships. The Board should consider other alternatives available under the federal tax Code that would not require disruption of employment or co-employment relationships that have existed for many years and would not require CalPERS to deny benefits where contributions have been made for many individuals in good faith over a long period. The proposed regulation does not take into account these potential alternatives for dealing with current issues in this arena and it will not give CalPERS sufficient flexibility now or in the future.

Sincerely,

A handwritten signature in black ink that reads "Dennis Meyers". The signature is written in a cursive, flowing style.

Dennis Meyers  
Assistant Executive Director, Advocacy & Policy  
California Association of School Business Officials

cc: CalPERS Board of Administration  
Joe Parilo, Acting Regulations Coordinator



**Employer Services Division**

P.O. Box 942709

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December 9, 2008

Mr. Dennis Meyers  
Assistant Executive Director, Advocacy & Policy  
California Association of School Business Officials  
700 N. 10<sup>th</sup> Street, Suite 100  
Sacramento, CA 95811

Dear Mr. Meyers:

Thank you for taking the time to submit comments relating to the proposed regulatory action by CalPERS regarding determination of employee status. This letter is in response to the comments you submitted to CalPERS in your letter dated December 1, 2008. Each of your comments, as we understand them, will be restated below, followed by CalPERS staff's responses. Additionally, as your letter states that you concur with comments submitted by CCSESA on November 19, 2008, and by Scott Kivel on November 18, 2008, we are enclosing a copy of our responses to those comments for your information and because they may address some of your comments.

Your letter also includes three additional comments, two of which suggest that you believe the proposed regulations should be expanded beyond determination of employee status to include co-employment and participation of non-public entities in governmental plans, and one that suggests a manner of correcting past erroneous reporting. Each of your additional comments followed by CalPERS staff's response is set forth below:

**Comment 1.** Expand the Regulation to Include the Co-Employment Topic. The proposed regulation does not take into account potential co-employment situations that already exist in California and does not leave CalPERS sufficient discretion to deal with these existing situations and similar circumstances that may arise in the future.

**Response to Comment 1.** CalPERS staff disagrees with your suggestion that the proposed regulation be expanded to take into account co-employment.

You failed to identify any specific "existing situations" or to indicate how co-employment would apply in these situations. After review of the IRS authority cited in your letter,<sup>1</sup> we conclude that the cited authority is not germane to the proposed regulations; the co-employment concept arises in different circumstances for different purposes than CalPERS membership eligibility under the Public Employees' Retirement Law (PERL) and is beyond the scope of the proposed regulations for reasons including, but not necessarily limited to, the following:

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<sup>1</sup> Chief Counsel Advice Memorandum 200415008, which cites Revenue Ruling 66-162.

1. CalPERS is bound to follow the applicable law on qualification for CalPERS membership. The proposed regulation clarifies, interprets and applies the PERL, the case law and the Board's Precedential Decisions concerning employee status under the common law test for employment.
2. The cited authority discusses co-employment solely in the context of determining an employers' liability to pay federal employment taxes on behalf of its common law employees. It does not discuss co-employment in the context of membership eligibility under the PERL, or in the context of which employer may be eligible to contract with CalPERS to enroll its employees.
3. The cited authority discussion on co-employment comes up only after the common law employment test has been applied to establish the employer-employee relationship with more than one employer.

**Comment 2.** The Proposed Regulations Fail to Address Certain Employment Relationships. The proposed regulation does not take into account certain employment relationships that already exist in California and does not leave CalPERS sufficient discretion to deal with these existing relationships and similar circumstances that may arise in the future.

**Response to Comment 2.** CalPERS staff disagrees the proposed regulations should be amended to cover more than the determination of employee status under the common law test of employment. The proposed regulations have a limited purpose—making specific the criteria for employee determinations.

In addition to being beyond the scope of the proposed regulations, the suggestion that the regulations be changed to address "certain employment relationships" referred to in your comments is too vague for any action. The employment relationships are neither identified nor described in any detail, so it is not possible for CalPERS staff to discern what changes or additions you suggest to address your concerns. We have reviewed the IRS private letter ruling that you cited and note that the issue addressed in that private letter ruling<sup>2</sup> is different from and beyond the scope of the proposed regulations, as well.

**Comment 3.** Statement on Correction of Erroneous Reporting. Citing to the IRS Employee Plans Compliance Resolution System,<sup>3</sup> you assert that "To the extent that individuals who do not technically qualify as 'employees' under the definition proposed by CalPERS, these individuals are not required to be 'kicked out' of CalPERS to correct potential violations of the federal tax Code." You indicate that the IRS has procedures for governmental plan corrections in order to maintain tax qualified status. You then conclude that CalPERS may be allowed to correct "past eligibility errors by simply amending the retirement plan to include employees who were allowed to participate in error."

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<sup>2</sup> IRS Private Letter Ruling 9813019. The issue addressed was whether the status of a governmental plan would be adversely affected by covering employees of non-public entity employers.

<sup>3</sup> See Rev. Proc. 2008-50.

**Response to Comment 3.** We conclude that your comment does not suggest any changes to the proposed regulations and seems to be provided for information purposes on how CalPERS staff might correct past erroneous reporting of persons who are not entitled to CalPERS membership. We have reviewed the cited IRS revenue procedure, and it appears that the correction method referred to would not be applicable to the situation referred to in your letter.<sup>4</sup>

We hope this letter, along with the enclosures, helps you gain a better understanding of the proposed regulations.

Please note that a public hearing on the proposed regulatory actions by CalPERS which was originally scheduled for December 17, 2008, will be held on December 16, 2008, during the Benefits and Program Administration Committee Meeting scheduled to begin at 8:30 a.m., in the Lincoln Plaza North Auditorium at 400 Q Street in Sacramento.

Sincerely,

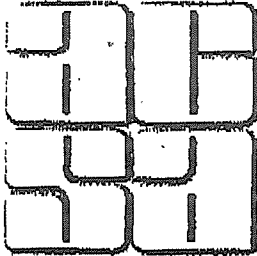


Lori McGartland, Chief  
Employer Services Division

Enclosures

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<sup>4</sup> We cannot determine from the information provided that the situation described would satisfy the specific requirements of the cited correction method at Rev. Proc. 2008-50, Appendix B, section 2.07(3)(a). Since the cited correction procedure is available only as to an operational failure of including an "otherwise eligible employee in the plan," and since the hypothetical facts in your letter provide that the individual would not technically qualify as an employee, it appears that this correction procedure would not be viable.



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December 1, 2008

Rob Feckner, President  
CalPERS Board of Administration  
P.O. Box 942701  
Sacramento, CA 94229-2701

Dear Mr. Feckner:

The Association of California School Administrators (ACSA), which represents 17,000 public school administrators, is providing public comment regarding the California Public Employees Retirement System (CalPERS) regulatory proposal to add Article 6.5 - "Membership" - to Title 2 of the California Code of Regulations.

ACSA is joining the California County Superintendents Educational Services Association (CCSESA) in objecting to CalPERS' proposed regulations defining common law employment for membership purposes. ACSA includes members employed under arrangements that include participation in CalPERS and therefore could be negatively impacted by the adoption of the proposed regulations.

ACSA concurs with CCSESA in that the CalPERS proposed regulations will do all the following:

1. The regulations fail to acknowledge longstanding statutory and co-employment relationships of County Superintendents, and will restrict the ability of the county superintendents to carry out their constitutional and statutory obligations as mandated by the Education and other California Codes and regulations.
2. The narrow application of such a regulation is likely to result in the exclusion of hundreds, if not thousands, of classified school employees in good standing that were heretofore reported, as required by law, as members of CalPERS, as well as other employees of cities, counties and special districts who will not meet the tests embodied in this regulation.
3. The regulation misapplies the findings of the Supreme Court case of *Cargill v. Metropolitan Water District* (2004) 32 Cal. 4<sup>th</sup> 491 to craft a narrowly drafted regulation intended to exclude employees from the CalPERS system.

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4. The regulation purports to clarify and interpret provisions of existing law that are not well defined, but instead vague and open to continuing subjective and selective interpretation by CalPERS staff charged with making determinations of employee status.

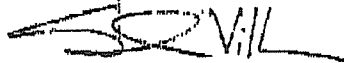
ACSA believes that if these proposed regulations are adopted they will disenfranchise those classified employees who have participated for years in good faith as members of CalPERS.

For these reasons ACSA urges the CalPERS board to reject the proposed regulations and, instead, direct staff to draft regulations that affirms, rather than denies, employment status and reorganizes the necessity and validity of statutory and co-employment relationships to the delivery of educational services by county superintendents of schools.

California public schools are operated through a maze of statewide, regional, local and extensive inter-agency collaborations that reflect how the state Legislature has directed locally appointed/elected officials to deliver educational services, develop programs, and provide monitoring and over-site services in an efficient and cost-effective manner. Because these proposed regulations conflict with longstanding statutory requirements and responsibilities related to the delivery of educational services by these appointed/elected officials, we concur with CCSESA that it places CalPERS' in the position of inadvertently dictating educational policy and practice through its regulatory interpretation.

ACSA requests that the CalPERS Board reject the proposed regulations and instead seek a full and accurate understanding of all the various employment relationships prior to adopting regulations which could impact the delivery of public school services throughout California.

Sincerely,



Sal Villaseñor  
Legislative Advocate

Cc: Members, Board of Administration  
Joe Parilo, Acting Regulations Coordinator



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December 9, 2008

Mr. Sal Villasenor  
Association of California School Administrators  
1029 J Street, Suite 500  
Sacramento, CA 95814

Dear Mr. Villasenor:

Thank you for taking the time to submit comments relating to the proposed regulatory action by CalPERS regarding determination of employee status. This letter is in response to the comments you submitted to CalPERS in your letter dated December 1, 2008. Each of your comments, as we understand them, will be restated below, followed by CalPERS staff's responses.

**Comment 1.** The proposed regulations "fail to acknowledge longstanding statutory and co-employment relationships of County Superintendents, and will restrict the ability of the county superintendents to carry out their constitutional and statutory obligations as mandated by the Education Code and other California Codes and regulations."

**Response to Comment 1.** CalPERS staff disagrees with your comment.

CalPERS did not include in the proposed regulations any discussion of statutory employment or co-employment because these topics are irrelevant to determining employee status and individual eligibility for CalPERS membership. If an individual is a common law employee of an employer that contracts with CalPERS, then that employee is eligible for membership (absent a specific statutory or contract exclusion from membership). That the employer may be the joint or co-employer of that individual with another employer, under a statutory scheme other than the Public Employees' Retirement Law (PERL), is irrelevant. Similarly, whether that employer has the general statutory authority to hire employees is also irrelevant to the common law test for employment analysis.

The proposed regulations require that the term "employee" be determined using the common law test for employment. The regulations clarify, interpret and apply the PERL, the case law and the Board's Precedential Decisions which set forth the applicable criteria of the common law test for employment.

The proposed regulations should not interfere with county superintendents carrying out obligations as mandated by the California Constitution, Education Code or other California codes and regulations because the regulations are solely drafted to apply to determinations made under the PERL.



The proposed regulations ensure that only the common law employees of an employer who has contracted to participate in the plan (regardless of whether that employer also has established a co-employment relationship with another employer for purposes other than under the PERL) are reported into membership.<sup>1</sup> CalPERS, as a tax-qualified governmental plan, may only provide pension benefits to a participating employer's common law employees and their beneficiaries. Thus, it is the common law test for employment that is determinative of employee status under the PERL.<sup>2</sup>

The Board has referred to the common law test for employment factors in two Precedential Decisions when examining questions relating to employee status for CalPERS membership eligibility.<sup>3</sup> Conversely, the Board has never issued a Precedential Decision recognizing "co-employment" or "joint employment" as a basis for CalPERS eligibility or as an exception to the common law test for employment. Nor has the Board issued a Precedential Decision determining CalPERS eligibility based upon an employer's general statutory authority to hire employees.

**Comment 2.** The proposed regulation will likely result in the exclusion of thousands of classified school employees in good standing that were heretofore reported, as required by law, as members of CalPERS, as well as other employees of cities, counties and special districts who will not meet the tests embodied in this regulation. You also contend elsewhere in your letter that the proposed regulation will disenfranchise those employees who have participated for years in good faith as members of CalPERS.<sup>4</sup>

**Response to Comment 2.** CalPERS staff disagrees with your comment. The proposed regulations will not eliminate CalPERS eligibility for membership for CalPERS participating employers' common law employees. To the extent that individuals are not the common law employees of CalPERS' employers, they will have been reported as CalPERS members in error. Where CalPERS discovers such errors in membership reporting, corrective action is taken on a case-by-case basis. If ultimately a determination is made that an individual fails to qualify for CalPERS membership under the common law test for employment, then service credit must be backed out and member contributions refunded.

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<sup>1</sup> This is consistent with the California Supreme Court's discussion of this issue in *Metropolitan Water District of Southern California v. Superior Court* (2004) 32 Cal.4<sup>th</sup> 491, 506 (also referred to as *Cargill*).

<sup>2</sup> See *Cargill*, *supra*, 32 Cal.4<sup>th</sup> 491..

<sup>3</sup> See *In the Matter of the Application for CalPERS Membership Credit by Lee Neidengard v. Tri-Counties Association for the Developmentally Disabled*, Precedential Case No. 05-01 (2005) (*Neidengard*), and *In the Matter of the Application to Contract with CalPERS by Galt Services Authority*, Precedential Decision No. 08-01 (2008) (*Galt Services Authority*).

<sup>4</sup> These contentions rest on your bare assertion that large numbers of individuals currently being reported as CalPERS members will be excluded from membership eligibility as a result of these regulations. CalPERS staff disagrees with this assertion. No specific examples were provided to substantiate the assertion.

The proposed regulations have been promulgated to interpret the PERL, case law and Board Precedential Decisions which already use the criteria described in the proposed regulations to make employee and/or eligibility determinations for CalPERS purposes.

**Comment 3.** “The regulation misapplies the findings of the Supreme Court case of *Cargill v. Metropolitan Water District* (2004) 32 Cal.4<sup>th</sup> 491 to craft a narrowly drafted regulation intended to exclude employees from the CalPERS system.”

**Response to Comment 3.** CalPERS staff, again, disagrees with your comment. The regulations do not misapply the *Cargill* decision and were not drafted with the intent to exclude employees from the CalPERS system. As noted above, the proposed regulations require that the term “employee” be determined using the common law test for employment.

The regulations are authorized because Government Code section 20125 provides that the Board shall determine who are employees and is the sole judge of the conditions under which persons may be admitted to and continue to receive benefits under this system. The California Supreme Court in *Cargill* determined that the PERL incorporated the common law test for employment and referred to the common law test for employment factors identified in *Tieberg*<sup>5</sup>.

Although the Court in *Cargill* referenced the common law test for employment to provide CalPERS pension benefits to the common law employees of the Metropolitan Water District, CalPERS has also used the same test to determine employee status and eligibility and/or deny eligibility for pension benefits to any persons who are not the common law employees of a CalPERS employer. The Board recently discussed this in a Precedential Decision stating: “as the California Supreme Court held in *Metropolitan Water District v. Superior Court* (2004) 32 Cal.4<sup>th</sup> 491, 509 (*Cargill*), when determining whether individuals are employees of a public agency, CalPERS must apply the common law test for employment.”<sup>6</sup> The Board adopted the Administrative Law Judge’s decision upholding a CalPERS determination that the common law test for employment also may be used to deny pension benefits to any persons who are not common law employees of the employer.

**Comment 4.** The proposed regulation is vague and open to subjective and selective interpretation.

**Response to Comment 4.** CalPERS staff disagrees with your comment.

The proposed regulations incorporate the applicable common law factors used in determining employee status for CalPERS membership eligibility as discussed in the *Cargill* and *Tieberg* Supreme Court cases. The Precedential Decisions referenced

<sup>5</sup> See *Tieberg v. Unemployment Ins. App. Bd* (1970) 2 Cal. 3d 943 (*Tieberg*)

<sup>6</sup> See *Galt Services Authority*, supra, Precedential Decision No. 08-01 (2008).

above illustrate how the factors are to be applied when determining whether an entity is the common law employer of specific individuals.

CalPERS staff does not agree that the factors are vague or subject to arbitrary application. Rather, the factors have been discussed and applied by both the California Supreme Court and the Board in two Precedential Decisions.

We again thank you for your comments and hope this letter helps you gain a better understanding of the proposed regulations. CalPERS staff will be recommending the Board adopt the proposed regulations as drafted.

Please note that a public hearing on the proposed regulatory actions by CalPERS which was originally scheduled for December 17, 2008, will be held on December 16, 2008, during the Benefits and Program Administration Committee Meeting scheduled to begin at 8:30 a.m., in the Lincoln Plaza North Auditorium at 400 Q Street in Sacramento.

Sincerely,



Lori McGartland, Chief  
Employer Services Division